



INDONESIA: ECONOMIC AND FINANCIAL HIGHLIGHTS AUGUST 2005

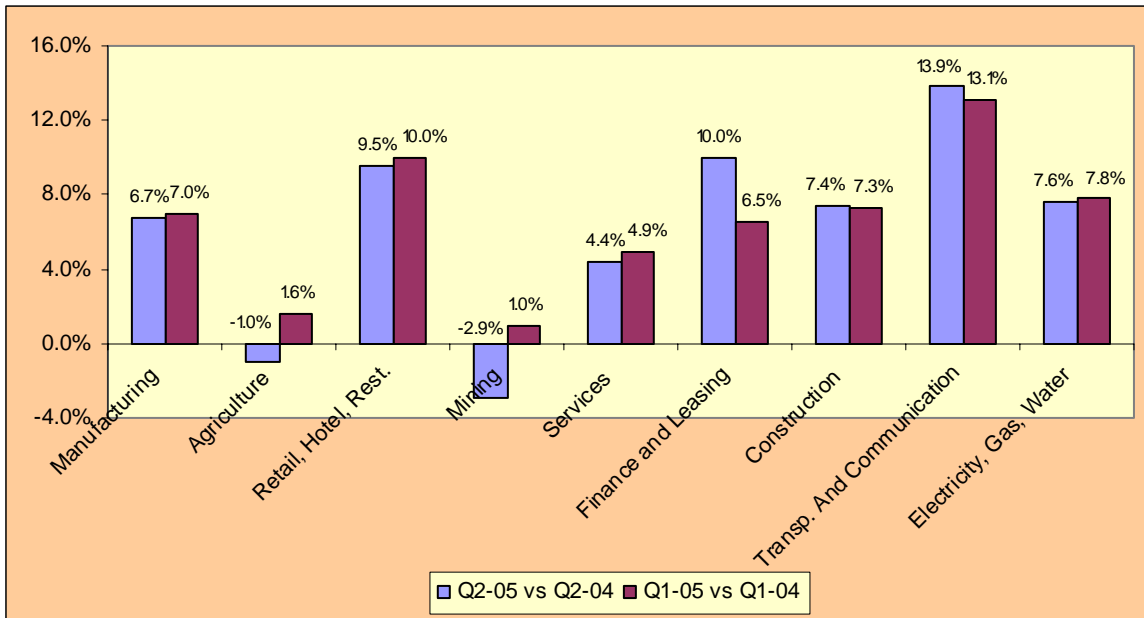
Summary:

- The Central Statistics Bureau (BPS) released figures on August 15 showing that economic growth in Indonesia slowed in the second quarter of 2005 to a 5.5 percent year-on-year (YoY) pace.
- Consumer price inflation rose in August 2005 to 8.3 percent YoY.
- The Indonesian rupiah sunk to its lowest rate against the dollar in four years, closing at Rp 10,870/USD on August 29.
- Analysts cited an overly accommodative monetary policy by Bank Indonesia (BI) and concerns over mushrooming fuel subsidies as the main concerns leading to pressure on the rupiah.
- BI raised its benchmark interest rate by a total of 125 basis points on August 30 and September 6 to bolster the rupiah.
- Despite sharply higher yields in the government bond market, the Government of Indonesia (GOI) issued Rp 1.6 trillion (USD 149.9 million) in 13-year rupiah bonds on August 30 at an average yield of 16 percent.
- The State Asset Management Company (PPA) completed the sale of the Government of Indonesia's (GOI) remaining 10.5 percent stake in Bank Danamon on August 3, raising Rp 2.7 trillion (USD 259.5 million) for the budget.
- The Capital Market Supervisory Authority (BAPEPAM) issued regulations on August 1 to facilitate more transparent over-the-counter bond trading.
- BAPEPAM also sent letters to more than 100 market players, including listed companies and investment managers, warning them against manipulation of financial statements and insider trading.
- The Ministry of Finance (MOF) reinstated the operating license of Tamporak Insurance, one of six insurance companies that had been forbidden to operate.
- Two major domestic banks, Danamon and Niaga, sold subsidiaries.

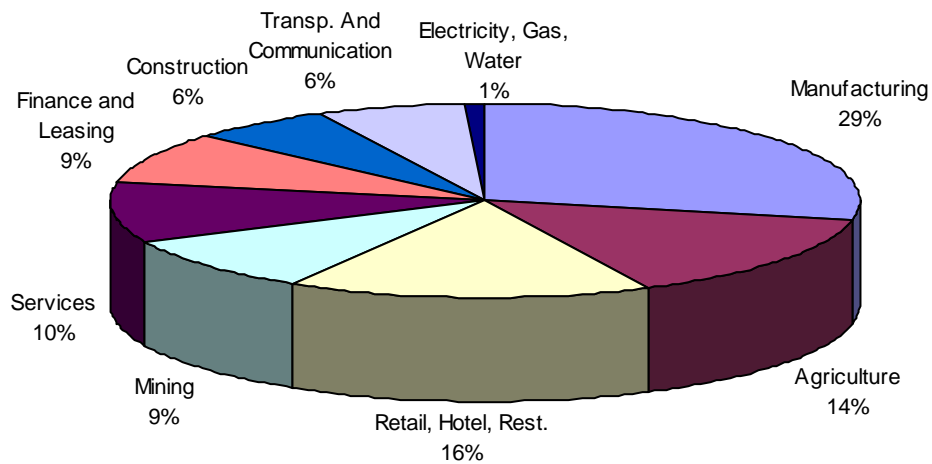
GDP Growth Slows in Second Quarter

On August 15, BPS announced that in the second quarter of 2005, Indonesia's economy grew 5.54 percent from the same period a year earlier. Growth slowed from the first quarter, in which GDP expanded at a 6.2 percent annual rate. Agriculture and mining slowed the most sharply from their Q1 rates (Table 1), with manufacturing, retail, and services also showing evidence of cooling. On the consumption side, Q2 results showed continued moderate growth in household consumption (3.5 percent YoY), while investment grew strongly for a third consecutive quarter at 13.2 percent YoY. YoY export growth also slowed significantly to 7.3 percent from its Q1 YoY increase of 13.4 percent.

**Table 1: Indonesian YoY Real GDP Growth:
Q2 2005 vs Q1 2005**



Share of GDP



B. Expenditure Category	Percent Change		Share of GDP
	Q2-05 vs Q2-04	Q1-05 vs Q1-04	
Household Consumption	3.5	3.2	64.6
Government Expenditure	-5.6	-8.5	7.0
Investment	13.2	15.0	21.5
Exports	7.3	13.4	33.0
Imports	10.1	15.4	30.1

Source: Central Bureau of Statistics (BPS)

Inflation Rose to 8.3% as Expected

On September 1, BPS announced that inflation rose to 8.3 percent year-on-year, and 0.5 percent month-on-month, roughly in line with expectations. Analysts cited a sharp, 3.29 percent increase in month-on-month education costs as the Indonesian school year began as the main factor driving inflation.

Table 2: CPI Components

Components	YoY	MoM
Food stuff	9.49	0.14
Food, beverages, tobacco, cigarettes	8.22	0.51
Housing, water, electricity, oil/gas	6.52	0.51
Clothing	5.46	0.43
Health	4.28	0.47
Education, recreation, and sport	8.53	3.29
Transportation, communication, financial services	12.17	0.09
TOTAL	8.33	0.55

Source: Central Bureau of Statistics

Rupiah Hits Four-Year Low Against Dollar

The Indonesian rupiah hit a four-year low against the U.S. dollar in the second half of August. On August 22 it closed above the psychologically important Rp 10,000/USD mark for the first time since March 2002. The currency's low point for the month came on August 29, when it closed at Rp 10,876/USD. Indonesia's stock and bond markets also declined in August. Morgan Stanley Capital International (MSCI) noted that by the fourth week in August, the Indonesian stock market had fallen 17 percent from an all-time high set on August 2. Government bond yields also increased sharply during the month (Table 3) in response to rising interest rates and deteriorating market sentiment.

Table 3: Government Bond Yields

Series	Aug 1	Sep 1
FR0002	11.71	14.86
FR0004	9.41	13.45
FR0013	11.21	15.42
FR0019	11.86	16.07
FR0023	11.53	14.86

Source: Bank Danamon, Citigroup

Most analysts attributed the broad deterioration in market sentiment in August 2005 to overly accommodative monetary policy in the face of rising inflation expectations and concerns over mushrooming fuel subsidies. Record world oil prices have led to unprecedented levels of GOI spending on domestic fuel subsidies, with

subsidies in 2005 projected to reach Rp 138.6 trillion (USD 13.2 billion) or approximately five percent of GDP. Heavy imports of refined fuel products estimated at USD 1.5-1.6 billion per month have also strained the foreign exchange market.

Government, Bank Indonesia Issue Policy Packages

Bank Indonesia announced several policy packages in August and early September designed to bolster the value of the rupiah. After its August 30 Board of Governors meeting, BI announced “immediate actions” and “short-term action plans” to respond to the rupiah’s decline. Immediate actions included raising short-term interest rates by 75 basis points to 9.5 percent and hiking BI’s rupiah deposit facility (FASBI) rate by 100 bps to 8.5 percent. In other measures to boost the rupiah, BI announced plans to issue regulations on margin trading in the FX market, banks’ net open positions and swap intervention. The August 30 policy package stabilized the market, with the rupiah closing at Rp 10,350/USD on August 31. BI raised short-term rates another 50 basis points to 10 percent on September 6.

President Yudhoyono also unveiled a GOI economic policy package in a televised speech to the country on August 31. The President stated that two key measures expected by investors--cuts in domestic fuel subsidies and a performance review of his cabinet leading to a possible reshuffling--would be taken after October. He added that the GOI would use the months of September and October to design and implement a program to compensate poor Indonesians who would suffer from higher fuel prices. The President stated he would not reshuffle his cabinet until he reviews the performance of Ministers after one year of service in October. Market reaction to the President's speech was mixed, with some analysts suggesting it did not go far enough to address ballooning fuel subsidies and other fiscal issues.

GOI Issues Rupiah Bonds in a Tough Market

The MOF issued Rp 1.6 trillion (USD 149.9 million) of 13-year rupiah bonds on August 30 at an average yield of 16 percent. The yield was sharply higher than the 11.3 – 11.6 percent yield the MOF obtained at issuance for its June 2005 eleven and fifteen year rupiah bonds. MOF Director General for State Treasury Mulia Nasution said that despite agreement with Parliament to begin issuing T-bills in 2005, the GOI has been reluctant to issue the short-term bonds due to unfavorable market conditions. He also said the government will issue only fixed interest rate bonds in 2005.

Table 4: Government Bond Issuance Jan – Aug 2005

Month	Seri	Value (Rp trillion)
January	FR0027	5
February	FR0028	3
March	FR0028	Cancelled
April	FR0029	3
April *	INDO-15	9
May	FR0029 and FR0030	4.8
June	FR0030 and FR0031	3.8
July	FR0031 and FR0032	Cancelled
August	FR0032	1.6
TOTAL		30.2

(*) USD 1 billion international bond issue.

Source: *Investor Daily*

Another USD Bond Issue in the Works?

With yields for rupiah bonds rising sharply, the MOF signaled plans to tap international capital markets for a second time in 2005. “We have invited international investment banks to advise on a sale,” Rahmat Waliyanto, a director of MOF’s debt management unit reportedly said. Waliyanto declined to comment on the size of a second GOI bond in 2005 or the time frame for the issuance.

Rising interest rates are also beginning to impact on the budget. Director General Nasution told the press that a one percent increase in the interest rate on Bank Indonesia Certificates translates into an additional Rp 2 trillion (USD 192.2 million) in GOI spending on interest on outstanding debt. (Note: One-month SBI rates have increased by 258 bps this year.) Nasution added that macroeconomic conditions must therefore be considered in decision-making about bond issuance for the remainder of 2005. Parliament approved the issuance of Rp 43.3 trillion (USD 4.2 billion) in GOI bonds in 2005 to finance the state budget. So far in 2005, the GOI has raised approximately Rp 30 trillion (USD 2.8 billion) from the sale of bonds.

Government Sells Bank Danamon Shares

The GOI announced on August 3 it had sold its remaining 10.5 percent stake in Bank Danamon Indonesia, the nation's fifth-largest lender by assets, at Rp 5,200 per share, raising Rp 2.68 trillion (USD 257.6 million). “The Bank Danamon stake sale shows that the market is positive about the investment climate in Indonesia,” Mohammad Syahrial, the president of State-Owned Asset Management Company Perusahaan Pengelola Asset, or PPA, said in a written statement. Syahrial said that the price reflected 3.27 times Bank Danamon's price-to-book value as of December 31, 2004. The Parliament raised concerns that the sale price was somewhat below the closing market price (Rp 5,200 versus Rp 5,300).

With the sale of the GOI's remaining stake, Asia Financial Pte. (controlled by Singapore's state-owned investment company Temasek Holdings Pte.) owns 65.75 percent of Danamon, while 23.75 percent is publicly held. Sources in the banking industry said Temasek may increase its stake to around 69 percent after the PPA sale, which was mostly dominated by foreign funds. The GOI plans to sell its remaining five percent stake in Bank Central Asia, the nation's second-largest lender by assets, later this year.

New BAPEPAM Regulations for GOI Securities

Responding to the difficulties in obtaining consistent bid-ask prices for GOI bonds, on August 1 BAPEPAM issued a new regulation on the fair value of government bonds. The regulation is designed to standardize pricing of GOI securities traded over the counter (OTC) and strengthen legal certainty for purchasers. Price calculations now must refer to price information provided by the Inter Dealer Market Association (IDMA). Based on the new regulation, the IDMA is required to report the fair market value of government bonds to BAPEPAM on a daily basis. Mutual fund managers must use the fair value for government bonds held in mutual fund portfolios based on the IDMA reference price, with allowances made for some variation depending on the maturity dates of bonds. Additionally, the new regulation requires mutual fund managers to use the IDMA reference price to calculate the daily net asset value (NAV) for mutual funds.

BAPEPAM Sanctions 104 Market Players

On August 10, BAPEPAM announced that it had imposed administrative sanctions (fines) against 94 listed companies and 11 investment managers. Total penalties reached Rp 3.7 billion (USD 0.4 million). Two cases have been the focus of public attention: manipulation of financial statements and a bond default by garment manufacturer Great River International, and allegations of insider trading in a share buy-back program by Indonesian baby and nutrition food manufacturer Sari Husada. BAPEPAM has been investigating the cases for some time, with some analysts criticizing the slow pace of evidence gathering. The Jakarta Stock Exchange suspended Great River in February 2005.

Insurance Company License Reinstated

After two years in limbo, the Ministry of Finance reinstated the operating license of Tamporok Life Insurance Company, a small domestic insurer. On August 9 the MOF announced it considered Tamporok's takeover by an undisclosed domestic insurance company "to be positive". The MOF is currently reviewing the operating licenses of five other insurance companies.

Insurance Company Pays Claims for Tsunami Damage

On August 10, insurance company Wahana Tata and cement company Semen Andalas signed an agreement on the cement company's tsunami claim payment of EUR 50 million (USD 61.1 million). Coordinating Ministry for Economic Affairs Aburizal Bakrie witnessed the signing. Semen Andalas registered a total loss of USD 90 million due to the tsunami disaster.

Bank Danamon Refinances Debt, Sells Subsidiary

On August 12, natural resources and industrial management company Prasadha Aneka Niaga announced that it has completed a USD 9.3 million debt refinancing transaction with Bank Danamon, Indonesia's fifth largest commercial bank. The transaction was completed after Danamon secured a USD 11 million loan from a Cayman Islands exempted partnership, ADM Maculus Fund.

On August 15, Bank Danamon signed a "Conditional Sale and Purchase of Share Agreement," completing the sale of its 15 percent stake in PT Korea Exchange Bank Danamon (KEBD) to PT Clemont Finance Indonesia (Clemont). KEBD was a joint venture bank, owned by Korea Exchange Bank Seoul and Danamon, with assets of Rp 2.2 trillion (USD 211.4 million). Clemont Finance is a subsidiary of the Korean conglomerate Korindo.

Niaga Sells Ownership in Securities Company

On August 16, PT Bank Niaga sold its 48 percent stake in PT CIMB Niaga Securities to its joint venture partner, Commerce International Merchant Bankers (CIMB), a wholly owned subsidiary of the Malaysian Berhad group for 10.58 million Malaysian Ringgits (USD 2.8 million). After the sale is complete, CIMB intends to merge PT CIMB Niaga Securities' operations with a second securities firm in which CIMB also owns a stake, PT GK Goh Indonesia. Under BAPEPAM rules, corporate groups are not permitted to hold equity interests exceeding 20 percent in more than one licensed company involved in the securities industry.

Multifinance Company Launches IPO

On August 23, Mandala Multifinance launched an Initial Public Offering (IPO) of 325 million shares at Rp 195/share. The IPO was almost two times oversubscribed, and raised Rp 120 billion (USD 11.5 million) in capital for the firm. Mandala finances motorcycles produced by Yamaha, Honda, Suzuki, and Kawasaki through a network of 43 branches and 650 dealers in 15 provinces. Domestic demand for motorcycles has grown more than 30 percent in the past year. Currently there are eight financing companies listed in the Jakarta Stock Exchange.

Selected Economic, Monetary & Financial Statistics

	May 05	Jun 05	Jul 05	Aug 05
CPI Inflation (YoY)	7.40	7.42	7.84	8.3.33
CPI Inflation (MoM)	0.21	0.50	0.78	0.55
Rp/USD Exchange rate ¹	9,480	9,713	9,819	10,350
30-day SBI Interest Rate ²	7.90	8.25	8.49	9.51
Foreign reserves ³	34.61	33.86	32.10	32.02
JSX Composite Index	1088.2	1122.4	1182.3	1050.1
JSX Trans Volume ⁴	1,339	1,209	1,657	
Exports (USD billion)	7.21	6.73	6.99	
% Change (YoY)	30.79	27.48	25.85	
Import (USD billion)	4.96	4.72	4.82	
% Change (YoY)	37.18	35.35	31.89	
Trade Balance ⁵	2.25	2.01	2.17	

Source: Bank Indonesia, BPS

(1) Rp/USD, end of period

(2) End of period

(3) USD billions, end of period

(4) Jakarta Stock Exchange average daily transaction volume, in billions of shares

(5) USD billions

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